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SUBJECT: RESPONSE: IMPACT OF RISING FOOD/COMMODITY PRICES -
GERMANY

REF: SECSTATE 39410

11. (U) Summary: The recent press coverage of rising food prices has prompted the German Government to review its current policies affecting food and feed supplies. Domestically, there are a variety of factors contributing to rising food and feed prices. As expected, farmers have responded to higher commodity prices and have or are planning to expand output. Specifically, Germany's biofuels policy is coming under fire and receiving increased scrutiny. Germany recently increased its pledges to the World Food Program.
End Summary.

12. (U) Agricultural and Food Demand: The German food and agricultural industry is in general self-sufficient with net imports only for protein meals, fruits and vegetables, fish, vegetable oils, eggs and to a lesser extent pork and poultry. Primary suppliers are neighboring European countries and to a growing extent countries such as Brazil, Argentina and Thailand. In general, food prices in Germany rose in 2007 as a result of increased demand on the world market and reduced domestic supplies for grains and oilseeds. The largest food price increases were observed in the dairy sector. For example, prices for fresh full-cream milk jumped 31 percent. (However, Aldi, a leading discount retailer which often sets the trend in milk prices, reduced them last week.) Consumers also paid more for other products such as fruits (+11 percent) and bread and cereals (+9 percent). In contrast, prices for pork products have remained relatively stable due to large market supplies.

13. (U) Despite the overall price increase, it does not appear that German consumers have significantly altered their food consumption patterns and have largely accepted the current situation. On average only about 12.5 percent of Germans disposable income is spent on food, thus, the issue of rising food prices has not yet significantly cut into consumers' pocketbooks.

14. (U) The demand impact of biofuels, predominantly biodiesel, on vegetable oil market has grown in Germany over the past 5 years. Biodiesel currently accounts for about 50 percent of total vegetable oil demand (from both domestic and imported sources). This has increased from about 30 percent five years ago. The viability of this market is currently under assault from reduced tax breaks, imported biodiesel, and the relative prices of petroleum and vegetable oil. There are also growing public sector and NGO concerns about the impact of this demand on food prices.

15. (U) Supply: Market prices received by farmers have influenced land and crop allocation in Germany over the past several years. Given the bright outlook for biodiesel in Germany and surging prices in 2006, farmers planted a relatively larger area (approximately 110,000 hectares or about 8 percent) of winter rapeseed at the expense of grains. In making winter planting decisions in 2007, farmers switched an equivalent amount of area (110,000 hectares)

from oilseed production back into grains. In addition, the elimination of the set-aside requirement brought about 200,000 hectares of land into production with a majority returning to grain or silage production. Current weather prospects indicate a significantly increased grain crop in Germany for 2008. In the livestock sector, relatively high milk prices in 2007 encouraged herd expansion and increased milk production. As a result, milk prices have begun to fall to farmers and to consumers.

¶6. (U) Germany no longer has sizable public-owned commodity stocks to buffer the market from price fluctuations. Since reform of the Common Agricultural Policy, Germany reduced its publicly held stocks to almost zero. This has resulted in a rise in the market importance of privately-held stocks and increased price variability.

¶7. (U) The high price of petroleum products has impacted the cost for transportation and the processing of input materials (i.e. energy and fertilizers). However, reports indicate that farmers have been maximizing the use of inputs in 2008 in order to increase yields to the maximum and reap the benefits of higher prices.

¶8. (U) The EU's agricultural biotech policies have increased animal feed costs for the German livestock industry. This has been due the inability to import corn and corn gluten feed from the United States and increased demand for corn from those suppliers only producing EU-approved events.

¶9. (U) POLITICAL IMPACT: During the fall of 2007, increasing food prices, particularly dairy, caught consumers' eyes and were cited by some labor unions as an additional reason for wage increases in contract negotiations, but overall did not result in any noticeable political impact. However, front page coverage of the global food market conditions, as well as a growing debate over the negative environmental impact of some biofuels, has fed a public perception

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that biofuels are a major cause of rising global food prices, especially in developing countries. German politicians and government officials are increasingly positioning themselves to appear responsive to these concerns. Most notably, Environmental Minister Sigmar Gabriel (Social Democratic Party), recently launched a review of the current biofuels policy. Others, such as Christian Democratic Union/Christian Social Union Bundestag faction leader Volker Kauder, are calling for a re-evaluation of German and EU policies regarding the use of new technologies in farming.

¶10. (U) Economic Impact: In 2007, Germany's inflation rate climbed to 2.2 percent, the highest level in 13 years. Higher costs for food, fuel and energy largely accounted for this increase. Although consumers spent more on staple products recently, no dramatic food substitution has occurred. Rising food prices contribute to the debate over whether social inequality is rising in Germany. Some observers argue that past wage moderation has caused a decline in real incomes, especially among low-wage groups who are disproportionately affected by food price increases. However, with only an average 12.5 percent of disposable income spent on food in Germany, the increases have not yet significantly affected consumers' pocketbooks.

¶11. (U) Environmental Impact: There have been no reported impacts from the elimination of set aside requirements for farmers. However, there has been an increase in the use of farm chemicals in the past year to take maximum advantage of production potentials.

¶12. (U) Government Policy Response: On April 21, the German Government created a "Food Crisis Task Force." The group consists of high-level members of the ministries of Agriculture, International Development, and Economy, under the leadership of the Chancellor's Office. The Task Force is charged with reviewing all German policies that might be contributing to increased food prices including biofuels and agricultural biotechnology. The first outputs from this discussion are expected to be available prior to the G-8 Summit.

¶13. (U) During the past year, German agricultural, food and feed

industry representatives have been warning the German Government that the EU policy on biotechnology may contribute to the rising of food production costs. German Agriculture Minister Horst Seehofer has a different view on this issues and has publically stated that industry statements about the potential market impact of not addressing the EU agricultural biotechnology regulatory system are overblown and that German and EU importers should work more closely with other grain producers such as Ukraine, Russia, and Brazil to meet import needs.

¶14. (U) In responding to international calls from additional resources for the World Food Program, Germany recently pledged an additional \$16 million on top of the estimated \$5 million it contributed in March. Normally, Germany's annual contribution to the WFP is estimated at \$36 million.

¶15. (U) Impact on Post Programs: Post has significantly increased attention to coordination efforts associated with international agricultural organizations including FAO and the Food Aid Convention. These efforts have paid dividends in creating consultation opportunities on important initiatives such as upcoming FAO conferences. Post continues to take advantage of Department programs such as the biotech outreach fund to share U.S. farmer experiences with biotechnology at a grass roots level. In FY 2007, three teams were funded to visit Germany. In FY 2008, two additional teams are expected.

¶16. (U) Policy Proposals: The creation of the Food Crisis Task Force provides an opportunity to establish a closer relationship on issues of U.S. interests with senior Germany officials on a wide range of policies that affect the global food/feed situation including FAO priorities, WFP needs and progress on the acceptability of agricultural biotechnology.

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